

§ 1.818-1

26 CFR Ch. I (4-1-14 Edition)

not modified when applied to non-equity-indexed MGCs. None of these sections are affected by the definition of current market rate contained in paragraph (a)(5) of this section once the temporary guarantee period has expired.

(5) *Examples.* The following examples illustrate this paragraph (b):

Example 1. (i) *IC*, a life insurance company as defined in section 816, issues a MGC (the Contract) on August 1 of 1996. The Contract is an annuity contract that gives rise to life insurance reserves, as defined in section 816(b). *IC* is a calendar year taxpayer. The Contract guarantees that interest will be credited at 8 percent per year for the first 8 contract years and 4 percent per year thereafter. During the 8-year temporary guarantee period, the Contract provides for a market value adjustment based on changes in a published bond index and not on the performance of stocks, other equity instruments or equity based derivatives. *IC* has chosen to avail itself of the provisions of these regulations for 1996 and taxable years thereafter. The 10-year Treasury constant maturity interest rate published for December of 1996 was 6.30 percent. The next shortest maturity published for Treasury constant maturity interest rates is 7 years. As of the end of 1996, the remaining duration of the temporary guarantee period for the Contract was 7 years and 7 months.

(ii) To determine under section 807(d)(2) the end of 1996 reserves for the Contract, *IC* must use a discount interest rate of 6.30 percent for the temporary guarantee period. The interest rate to be used in computing required interest under section 812(b)(2)(A) for 1996 reserves is also 6.30 percent.

(iii) The discount rate applicable to periods outside the 8-year temporary guarantee period is determined under sections 807(c)(3), 807(d)(2)(B), 811(d) and 812(b)(2)(A) without regard to the current market rate.

Example 2. Assume the same facts as in *Example 1* except that it is now the last day of 1998. The remaining duration of the temporary guarantee period under the Contract is now 5 years and 7 months. The 7-year Treasury constant maturity interest rate published for December of 1998 was 4.65 percent. The next shortest duration published for Treasury constant maturity interest rates is 5 years. A discount rate of 4.65 percent is used for the remaining duration of the temporary guarantee period for the purpose of determining a reserve under section 807(d) and for the purpose of determining required interest under section 812(b)(2)(A).

Example 3. Assume the same facts as in *Example 1* except that it is now the last day of 2001. The remaining duration of the temporary guarantee period under the Contract

is now 2 years and 7 months. The 3-year Treasury constant maturity interest rate published for December of 2001 was 3.62 percent. The next shortest duration published for Treasury constant maturity interest rates is 2 years. A discount rate of 3.62 percent is used for the remaining duration of the temporary guarantee period for the purpose of determining a reserve under section 807(d) and for the purpose of determining required interest under section 812(b)(2)(A).

(c) *Applicable interest rates for equity-indexed modified guaranteed contracts.* [Reserved]

(d) *Effective date.* Paragraphs (a), (b) and (d) of this section are effective on May 7, 2003. However, pursuant to section 7805(b)(7), taxpayers may elect to apply those paragraphs retroactively for all taxable years beginning after December 31, 1995, the effective date of section 817A.

[T.D. 9058, 68 FR 24350, May 7, 2003]

§ 1.818-1 Taxable years affected.

Sections 1.818-2 through 1.818-8, except as otherwise provided therein, are applicable only to taxable years beginning after December 31, 1957, and all references to sections of part I, subchapter L, chapter 1 of the Code are to the Internal Revenue Code of 1954, as amended by the Life Insurance Company Income Tax Act of 1959 (73 Stat. 112).

[T.D. 6558, 26 FR 2785, Apr. 4, 1961 as amended by T.D. 7469, 42 FR 12181, Mar. 3, 1977]

§ 1.818-2 Accounting provisions.

(a) *Method of accounting.* (1) Section 818(a)(1) provides the general rule that all computations entering into the determination of taxes imposed by part I, subchapter L, chapter 1 of the Code, shall be made under an accrual method of accounting. Thus, the over-all method of accounting for life insurance companies shall be the accrual method. Except as otherwise provided in part I, the term “accrual method” shall have the same meaning and application in section 818 as it does under section 446 (relating to general rule for methods of accounting) and the regulations thereunder. For general rules relating to the taxable year for inclusion of income